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BUDGET EXECUTION REFORM IN AFGHANISTAN

FINAL REPORT
SEPTEMBER 2012

September 2012

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DISCLAIMER

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LIST OF ACRONYMS

AFMIS	Afghanistan Financial Management Information System
ANDS	Afghan National Development Strategy
BPET	Budget Planning and Expenditure Tracking
CAO	Control and Audit Office
CBR	Capacity Building for Results
COA	Chart of Accounts/Chamber of Audit
COM	Council of Ministers
DAB	Central Bank
DANIDA	Danish International Development Agency
DFID	UK Department for International Development
GIROA	Government of Islamic Republic of Afghanistan
GFS	Government Finance Statistics
HR	Human Resource Management
IA	Internal Audit
IMF	International Monetary Fund
LOP	Life of Project
M&E	Monitoring and Evaluation
MAIL	Ministry of Agriculture Irrigation and Livestock
MIS	Management Information System(s)
MOE	Ministry of Education
MOED	Ministry of Economic Development
MOF	Ministry of Finance
O&M	Operations and Management
OJT	On-the-Job Training
P&G	Pay & Grading
PPU	Procurement Policy Unit
SBPS	State Budget Planning System
SDU	Special Disbursement Unit
SPU	Special Procurement Unit
USAID	United States Agency for International Development
USG	United States Government

EXECUTIVE SUMMARY

The budget execution system in Afghanistan has advanced markedly over the past several years in relation to core transparency, time-effectiveness and accountability standards. A well-organized and semi-automated budgetary financial management system (AFMIS) has been established which facilitates orderly processing and tracking of budgetary allocation, allotment, and payments processes at the national and sub-national level. Budget allotment and payment authorization procedures have been streamlined, and budget execution rates have improved during the most recent budget cycle. Basic financial and procurement planning and framework operational planning processes have been put in place in major line ministries/agencies; and this has improved the predictability and consistency of budget allotment planning and facilitated more accurate Treasury cash management processes.

In the broader budget control sphere, orderly and well-structured public procurement processes, broadly consistent with World Bank procurement guidelines, have been put in place in major line ministries/agencies. Basic transaction-based internal audit systems and processes have been established, and M&E units created and operationalized as well across major line units. Major progress has also been made in consolidated and “cleansing” employment records and reducing the prevalence of the “ghost employee” phenomenon, and considerable progress at the national level has been made in implementing comprehensive Pay & Grading (P&G) and job classification/evaluation schemes (most particularly in the Ministry of Education (MOE), which represents about two-thirds of the public sector workforce).

At the same time ongoing budget execution-related policy/regulatory and institutional strengthening gaps exist which need to be effectively addressed if the further significant improvements in budgetary transparency, time-effectiveness and accountability are to be achieved. These upgrading improvements are in turn critical if major donors are to gain greater confidence in the capacity of the budget execution system to effectively and transparently “absorb” the massive additional volume of on-budget donor financing resources recently discussed/agreed upon at the Tokyo Conference on Afghanistan’s development financing needs. Some of these reforms include regulatory and institutional strengthening measures which effectively represent the “inter-face” between budget planning and budget control, and are required in order to simultaneously promote greater rigor and transparency at “both ends” of the budget process.

Major areas of additional needed improvement include further streamlining of administrative approval processes (which still require 2 ½ - 3 weeks on average); and full integrated automation of core budget execution and related procurement and asset registry functions. In addition regulatory reforms which reduce uncertainty in the allocation of budget resources by program and province should be introduced; as well as basic cost/benefit and cost-efficiency principles which will introduce greater rationality into the development budgeting process, and simultaneously help discipline and better inform efficient project design and management planning and monitoring processes. Targeted technical/training support in these areas will be very important as well at the selected line ministry and provincial directorate level.

Technical/training support for the pilot introduction of risk-based financial and operational audit plans and methodological processes, as well as more meaningfully goal-focused M&E plans and measurement approaches, could prove extremely important from the perspective of effectively promoting enhanced budgetary accountability. Similarly, working with pilot line ministries to introduce and implement more detailed and rigorous procurement procedures/processes could have a significant demonstration effect-impact on promoting transformative procurement system reform in government. In addition, effective promotion of a final HR policy “push” for completing the payroll reconciliation and “cleansing” process, and development of a comprehensive plan for effectively integrating the large number of strategic donor-financed line staff within the permanent civil service compensation structure, are critically

important from a public service provision sustainability/efficiency perspective. Related technical support could prove critical for the development of well-focused and comprehensive HR training programs in key line ministries/agencies which create the basis for a sustainable post-donor personnel management and accountability-based service provision system in the GIROA.

In determining priority technical/training assistance areas it is critical to take effectively into account the pattern and impact of existing donor support programs in key budget execution areas. In this regard the donor community should focus on both providing support in key areas within major line/ministries agencies which have not been receiving adequate assistance in these areas (e.g. procurement and financial planning) up until now. Donor programs should however be ready to also look where needed to “top-off” support in line ministries or in centralized budget policy/ administration units (e.g. MOF in the AFMIS area) where an additional “push” may help reinforce and accelerate progress under programs initiated through existing donor programs. Support programs could be framed within the context of MOU-type agreements which help galvanize and transparently establish commitment on the part of relevant counterpart institutions to support forward-looking regulatory reform and institution-building progress in key budget execution areas. It could also entail donor-GOA agreements to move additional donor funding on-budget in accordance with demonstrated progress in key budget execution areas; which progress could in turn be supported/jumpstarted through targeted technical/training support initiatives.

Finally, in a general sense it seems clear that in most of the broadly defined budget execution areas covered in this report there is, not surprisingly, a much higher concentration of donor technical/training resources and support efforts at present at the central level rather than at sub-national levels. Moreover it appears that at least to some degree momentum is building for an institutional “push” to gradually focus greater implementation and oversight responsibility at the sub-national level; in a manner that better reflects local development needs and may better facilitate coordination of locally-implemented projects/programs. In light of these factors, donors should strongly consider a significant sub-national focus to its budget-execution related technical and training support initiatives in the future.

INTRODUCTION

In this paper we will examine the current core features of the Government of Afghanistan (GIROA) budget execution system; and discuss recent progress that has been made in the GIROA's pursuit of better practice budget execution policies and procedures. We will also assess/prioritize key remaining compliance gaps which need to be addressed for the GIROA to create a budget execution system which can meet the public service needs of its population, and which heightens the political visibility/legitimacy of the GIROA in their eyes. In doing so, we will explore the budget execution process at both the national and the provincial level (informed by site visits to Herat and Mazar-e-Sharif). Finally, we will put forward initial recommendations on priority areas of engagement for donors focused on fiscal reform issues to effectively promote additional budget execution reform progress; taking into account the reform plans/priorities of the GIROA in this area, and the current/prospective technical/training support programs of other major donors.

This analysis is based on a series of interviews carried out over the July 7 - 21 timeframe with relevant GIROA, donor, and USG officials involved in budget execution-related processes and/or support programs. It also reflects the results of site visits during that timeframe to two provinces – Herat and Mazar-e-Sharif – and related discussions with relevant Mustofiat, line directorate, Provincial Council, Development Committee, and NGO officials on budget execution-related topics. Our research at the line ministry/agency level focused predominantly on two major “prototype” line ministries – MOE and MAIL. The analysis herein provided starts with a brief contextualization of the under-appreciated importance of budget execution reform from a developmental and an enhanced political legitimacy perspective.

BUDGET EXECUTION REFORM - BACKGROUND

Budget execution system reform is critical to achievement of the sustainable socio-economic development and political stabilization goals of the GIROA and the international community. It is thus a fundamental reform requirement for the successful pursuit of the USG's foreign policy objectives in Afghanistan. This may at first glance seem a rather counter-intuitive proposition: budget execution tends to be viewed by non-practitioners as a dry, technocratic subject area. Making the system work “better” is seen as primarily entailing a focus on simplifying and re-ordering mechanical bureaucratic procedures and introducing automation systems which help better organize and process budgetary approval and payment transactions. This on the surface seems akin to a nuts-and-bolts organizational “reengineering” process; reform of which should be seen as a politically neutral objective which all those engaged in the public policy-making process should be easily able and ready to support.

However a closer look reveals that the core elements of the budget execution system – which establish the rules of the game and concrete processes through which budget allocation, allotment and payment actions are implemented – are critical for purposes of re-enforcing the political legitimacy of the public governance process with the Afghan populace. Budget execution reform is critical for purposes of improving the time-effectiveness and transparency characterizing budgetary allocations and actual expenditure levels and patterns. It also impacts on budgetary allocative efficiency, since it indirectly but powerfully influences the final allocation of fiscal resources post-Parliamentary approval of the annual budget. In addition it even impacts fiscal stability, since it powerfully influences the cost-effectiveness of expenditure programs and the ultimate funding requirements for the delivery of public goods and services.

Moreover the unique fiscal governance and deficit financing circumstances now facing Afghanistan amplify its impact on both the fiscal financing and the political legitimization side. In this regard a key fiscal financing and political self-determination goal of the GIROA is to move a significantly greater proportion of donor support funds from Afghanistan on-budget (currently around three-quarters of development assistance is reportedly provided off-budget).¹ This goal is shared with all major donors, and near-term commitment to it has been further reinforced by the reported agreements coming out of the recent Tokyo Conference on Afghanistan's fiscal sustainability needs and priorities.

However a key prerequisite for donors to place a larger fraction of their spending on budget – including from a statutory perspective - is a streamlined and more transparent and predictable budget execution process which will (1) protect the integrity of the financial resources made available to the GIROA; (2) ensure that it is allocated to broad programmatic areas which have been agreed upon in advance; (3) promote the time and cost-effective utilization of these resources; and (4) facilitate efficient post-expenditure reporting on how the funds have been utilized. If the budget execution system lacks these features, donors will in turn be unwilling and – depending on the types of deficiencies found – statutorily unable to increase the volume/share of resources placed on-budget.

All of these factors dramatically underscore the fundamental need for accelerated reforms in key budget execution areas. While achievement of this aim entails design and implementation of a significant number of “technocratically”-oriented bureaucratic process and related MIS improvements; it also entails critical policy reforms needed to facilitate more rational and equitable expenditure outcomes. Ultimately, the pacing and thoroughness with which these reforms are carried out will have reverberating impacts on both the level of budgetary resources made directly available by the external community; as well as its political legitimacy as a deliverer of critically needed public goods and services in the eyes of the Afghan people.

CORE ELEMENTS OF THE BUDGET EXECUTION PROCESS

The budget execution process entails three core elements which we will examine. These include:

1. **Budgetary Allocation:** The process by which the final assignation of annual expenditure resources is made, around the contours of the Parliamentary-approved budget (essentially the interface between the budget planning and budget administration system);
2. **Budgetary Allotment:** The process by which allocated funds are effectively made available for expenditure programs during the course of the fiscal year – critically important for purposes of budget predictability and time-effective delivery of services; and
3. **Budget Payment Authorization:** The process by which payments are approved/made to vendors providing public goods & services – fundamentally important from a service delivery efficiency and expenditure transparency perspective.

In addition there are a number of ancillary but important internal control-type functional areas which are extremely important to the integrity of the budget execution system. These include the Public Procurement process; the Monitoring and Evaluation (M&E) system; and the Internal Audit (IA) system. Each plays an important checks-and-balances role in ensuring the cost-effectiveness, programmatic impact, and the transparency of the budget execution system. In addition a sound Human Resource Management (HR) system is crucial for the cost-effective, efficient and motivated functioning of the public sector workforce, and in an indirect but powerful sense on the credibility and crisp and transparent operation of the budget execution system. The establishment of better practice standards

¹ IMF Staff Report, for the 2011 Article IV Consultation, November, 2011.

in each of these areas is a prerequisite for establishing the bureaucratic incentives needed in any country to help ensure that budgetary resources (own-sourced and donor-financed) will be prudently and transparently utilized. Progress in these areas is thus fundamentally important for purposes of achieving the shared goal of placing additional resources on-budget.

OVERARCHING BUDGET EXECUTION PROCESSES

FINAL BUDGETARY ALLOCATION

The budget execution process starts where Parliamentary approval of the annual budget ends (a flow-chart description of the budget planning and Parliamentary submission/approval process is provided in figure 1 of Appendix A). The Parliamentary approval process itself is typically an iterative 1-2 month process after the beginning of the fiscal year, which itself sets back basic budget execution timeframes. Following parliamentary approval of the budget – which for the development budget is currently provided at the institutional level but reportedly not at the program-level and not definitively by province); the budget is sent to the Council of Ministers (COM) for further de-composition. The approved allocations are then coded in accordance with a GFS-based (though not yet entirely consistent) Chart of Accounts (COA). At that point ministerial-level financial and procurement plans (informed by planning information at the provincial directorate level) are finalized/reviewed; and final allocation ceilings set.

BUDGETARY ALLOTMENT/PAYMENT AUTHORIZATION PROCESSES

The allotment process/cycle is described in figures 2-4, Appendix A. For the development budget, allotments are driven by the signature of contracts with vendors implementing GIROA or donor-financed projects (the 1391 capital budget is approximately \$1.1 billion, of which about \$2 million is own-source financed). In general annual allotments for newly signed contracts are made. Once the relevant line ministry makes a specific allotment request, there are multiple layers of review/approval of allotments against budgetary ceilings within the MOF; and final checks and entry into the Afghan Financial Management Information System (AFMIS) is done by Treasury. Allotments for on-going projects are made on a periodic basis based off of the aforementioned annual financial and procurement plans. Allotments for goods & services are generally made on a quarterly basis (again based off of the financial and procurement plans) and in accordance with a streamlined allotment review/approval process. Allotments for wages & salaries are based off of extent payroll records and are again processed on a quarterly basis. Allotments for provincial-level ministerial units are transferred to local branches of the Central Bank (DAB) under the custodial control of the Mustofiats (MOF offices) in each province.

Payment authorization processes are described in figures 5-6 of Appendix A. Payment form requests (M-16 forms) are processed through the relevant line unit, reviewed by the MOF financial controller in each line ministry, and then upon approval passed to the Special Disbursement Unit (SDU) in Treasury, subsequent to which a final compliance review and check against the allotment balance is carried out by MOF. The approved funds are then transferred to a vendor account. This describes the payment process for projects which are directly overseen by the central line ministries.

For projects which are implemented/overseen at the provincial level, the final MOF approval is followed by the notification of the provincial Mustofiat and the transfer of funds to a provincial DAB account for development projects held by the Mustofiat in a provincial DAB account. At that point the relevant provincial line directorate passes a direct request for payment to the Mustofiat, which processes the

request and upon approval issues a check to the provincial DAB branch in the vendor's name. Payment authorization processes for "local" goods & services and for local salaries are processed directly between the relevant provincial line directorates and the Mustofiat.

ANCILLARY BUDGET EXECUTION PROCESSES

The public procurement process is governed by the following general framework: Procurements under \$10,000 require a 'shopping' procedure involving at least 3 bidders. All procurement above this level requires the establishment of a formal evaluation committee. There are well-organized bid advertisement, bid opening, and bid evaluation procedures. The nature of the bid evaluation process is determined by the type of procurement under review (works, goods & services, consulting services). The results of the evaluation committee review are then provided to a ministerial level review/approval committee for final approval. An organized appeals process exists, whereby a bidder has 14 days to submit an appeal to the Procurement Policy Unit (PPU) in the MOF. Large-scale project procurement actions (over approx. \$ 5 million) are directly undertaken by an inter-ministerial Special Procurement Unit (SPU) overseen by the PPU. The PPU also is charged with providing procurement outreach/training support for the procurement units set up by each line ministry. The overarching public procurement law and related regulatory framework have been put in place with the support of the World Bank, and are based on World Bank procurement guidelines.

Provincial procurements can be carried out by line directorates for "shopping" actions up to approx. \$3,000. Procurement action from \$3,000-\$10,000 can be carried out through a process led by a committee established at the provincial governorship level. Provincial Governors have been assigned recently the right to establish committees to oversee capital project procurements up to approx. \$900,000 in value; although this policy has reportedly not yet been implemented (it was put in place in 1390 by Presidential Decree).

The Monitoring & Evaluation (M&E) process within the GIROA appears to be largely driven by the centralized unit established within the MOF. This unit, staffed with a skilled group of embedded donor-financed advisory staff, has developed a focused and ambitious M&E training/outreach and quality review/assessment role through which it works with M&E Units at the line ministry/agency level to both build capacity and ensure that comprehensive and meaningfully articulated M&E plans are put in place across all major sectoral areas. The plans with more advanced ministries are typically tied to and organized in a manner consistent with overarching operating plan frameworks and related program budget structures and performance goals/targets; with the more advanced ministries having put reasonably comprehensive/systematic M&E game-plans in place.

The M&E staff in the more robustly staffed units undertakes rotating trips to the provincial level to review/assess progress with provincial directorate staff and with provincial level M&E officers. Periodic training activities are also carried out by the centralized M&E teams in advanced units such as MOE and MAIL, each of which reports on results directly to the Ministerial level. Again embedded advisory teams seem to be driving the process in a number of higher profile line ministries, including MOE and MAIL. Availability of robust data relevant for purposes of developing benchmark data and setting relevant performance goals remains a critical challenge, although the program budget development process has helped provide a strong additional nudge for progress in this direction. Overall it seems clear that increasingly explicit donor-driven focus has been placed on development of more transparent M&E processes and informational networks over the past several years.

The Internal Audit (IA) process is of fundamental importance from the perspective of promoting basic accountability for the cost-effective and efficient delivery of public goods & services. The MOF's

centralized IA Unit, supported through U.S. Treasury advisory services, has both developed a basic IA annual plan for the MOF and also initiated limited outreach efforts designed to promote the development of organized IA plans and to promote capacity development in selected line ministries/agencies. The IA unit in the MOE is also supported by embedded donor advisors, and provides targeted training in internal audit planning and methodological approaches to the permanent staff of the unit. The MOA Internal Audit Unit appears to be more skeletal in nature; and the leadership of the ministry reportedly has developed plans to effectively “farm-out” core IA functions to commercial accounting/audit companies.

It appears at this point in time that the IA upgrading process remains at a nascent stage of development. The audits carried out by the IA Office in the MOF and other IA line units are “transactional” in nature, and do not focus on even the most basic type of performance auditing; nor do they focus in a meaningful way on financial audit analysis. Annual audit plans are not risk-based; and anecdotal evidence/observation indicates that IA units do not appear to have assumed a high-profile status in most line ministries/agencies. The units also appear to be under-staffed and under-financed to undertake required field-based audit work.

There seems to be some degree of uncertainty inter-institutionally regarding the relative sphere of responsibility of IA units in relation to the Chamber of Audit (COA), which reports to the Parliament and which undertakes external audit activities. In this regard the COA at times appears to provide direct guidance to IA units in their audit plans. The good news is overall is that there has clearly been an enhanced focus over the past few years on establishing functioning IA Units across a large number of line ministries/agencies; again largely supported by embedded donor-funded advisors. The units are fragile and understaffed/trained, but a start has been made.

The Human Resource (HR) Management system in the GIROA has taken major strides towards enhanced transparency and efficiency over the past few years. The HR Unit in the MOF and those in more progressive line ministries have taken major steps towards developing centralized personnel data bases and “cleansing” personnel records by comparing these ministerial “census” figures on employment against payroll records. In addition systematic Pay and Grading (P&G) and related job classification and employee evaluation reforms are being introduced at the line ministry/agency level. E-attendance systems are being increasingly adopted to control more effectively for absenteeism, including a biometric daily registration system in MAIL.

The MOE and MAIL HR Units have reportedly each eliminated approximately 1,000 ghost employees already through these reforms, and have comprehensively introduced P&G reforms. In the case of the MOE – which represents about 2/3rds of all government staff; the P&G system now covers 206,000 out of a total of 248,000 employees, with the remaining employees to be covered by the end of 1391. MAIL has reportedly developed a gender-focused recruitment and training unit – a major step forward. Again policy and institution-building support appears to be provided in high profile ministries largely by embedded donor-financed staff.

BUDGET EXECUTION REFORM – MAJOR AREAS OF RECENT PROGRESS

The GIROA has taken major steps forward in development of a more transparent, time-effective and efficiently integrated budget execution system over the past few years. The AFMIS system has been anchored for the past half-decade by the Free-Balance General Ledger Module. Over the past two years real time connectivity has been achieved with line ministries/ agencies and provincial Mustofiats. This has facilitated real time data entry/transfer between line units and the Treasury for operating expenses. It has also facilitated more predictable and time-effective budgetary transfer flows between the Treasury and provincial Mustofiats. In addition there have been focused efforts to reduce the burden of paper-based signatures required to push through allotment and payment authorization approvals within line ministries and in the MOF. Budgetary allotment and payment transfers operate through a unified treasury single account-based system.

Moreover the introduction this past year of comprehensive annual financial and procurement plans at the line ministry/agency level at the beginning of each fiscal year has significantly improved the degree of organization and accuracy characterizing allotment processes and facilitated more effective cash management planning by the Treasury. In addition the implementation of functional budget planning/tracking software in the MOF (SBPS system) and in a number of major line ministries (e.g. MOE and MAIL each utilize the BPET system) has facilitated more efficient and time-effective transmission of budgetary transfer requests between line units and the Treasury than was previously the case. At the same time major institution-building efforts have been undertaken to train-up budget execution staff at the MOF and the line ministry/agency level, again largely through the utilization of embedded donor-financed staff. As a result of this network of institutional reform and capacity-building measures the execution rate for the operating budget reached approx. 94% in 1390; while the execution rate for the development budget rose from an utterly anemic 39% in 1389 to about 52% in 1390. The goal of the Treasury Unit is to increase that rate by at least 10% annually over the coming years.

More organized operational planning processes are being implemented across line ministries, thus promoting more effective/accurate formulation of budgetary need estimates as well as tying into more effective M&E and internal audit game-planning activities. The more advanced ministries (e.g. MOE) are providing training on risk-based audit approaches, and M&E plans are becoming more strategic and goal-focused than previously through their increasingly direct linkage with program budget processes and indicators and through accompanying training on M&E plan formulation.

In addition, HR reforms continue to accelerate as noted above – particularly at the national level - with plans to accelerate the development of centralized personnel data bases and effectively address ghost employee issues at the provincial level as well. In this regard the MOE has initiated the process of sending personnel records to each province for checking against payroll records, with the goal of completely “cleansing” personnel and payroll files and eliminating the ghost employee issues by 2013. In addition new self-assessment based evaluation system reforms are beginning to be introduced in vanguard ministries (e.g. MOF, MOE); and staff training needs assessments are reportedly being expanded in more progressive ministries down to the provincial level.

BUDGET EXECUTION REFORM - STRATEGIC POLICY/INSTITUTIONAL GAPS

Despite the considerable progress which has been made towards establishment of a more transparent, time-effective and efficient budget execution system and related institutional architecture; there remain a number of critical gaps in the policy and institutional framework which need to be addressed in order to meet the GIROA and the donor community's core budget transparency and rationality goals. A number of these reforms are also quite important from the perspective of placing the donors in a statutorily viable and politically defensible position to put a significantly larger fraction of their developmental resources on-budget than they are currently doing. In the absence of these shifts in the budget execution system, it will likely prove difficult to ensure the strong linkage between budgetary resources and time-effective and efficient delivery of public goods & services so critical to the political stabilization goals of the GIROA and international community; and to widening the on-budget availability of donor funds. These critical constraints are enumerated below:

CORE BUDGET EXECUTION PROCESSES

In spite of the impressive recent progress cited above, core budget execution processes remain excessively time and paper-intensive. Although the development budget execution rate has risen to 52% this past year, this still represents sluggish performance in relation to (1) the overwhelming socio-economic development needs of the Afghan population; and (2) the expenditure time-effectiveness requirements likely to be expected by donors who are being asked to put massive additional amounts of donor funding on-budget during the next few years. Since these expenditure rates reflect spending out of current year budgetary allocations rather than LOP funding, they presumably can/should be significantly improved.

In terms of the mechanics of the budgetary transfer process, the allotment approval cycle continues to have duplicative elements which could be further streamlined. It appears that essentially duplicative review processes are conducted in the sectoral budget office and also by the Budget Execution Department within MOF, and that the registration of allotment approval documentation through the archive office fills no meaningful/necessary bureaucratic purpose (other than meeting a formal procedural requirement) that could not be fulfilled in other ways. Overall there are reportedly up to 14-16 signatures required for one development funding-related budgetary allotment action; and the entire process can easily take from 2 ½ to three weeks. If key signatories are absent for lengthy periods of time, the process can take even longer.

While the payment authorization process is not quite as paper-intensive, it still requires 7-9 signatures per action, and again can easily require 2 or more weeks to complete. Unlike the budget allotment process for development funds, which virtually always occurs at the center; payment authorization processes are carried out at the provincial level as well for locally-executed projects, and the Mustofiat offices have yet to eliminate duplicative steps that artificially lengthen the payments process at the sub-national level. Overall there appear to be significant additional efficiencies which can be gained from further streamlining of paper approval processes for budgetary allotment and payment authorization actions.

In addition the lack of more integrated automation of core budget execution processes still hampers time-effective and transparent budget approval actions for the development budget. Up until recently the processing of development budget allotment and payment processing actions continued to be done via paper approval routes; since the Treasury found that error rates were too high to warrant activation of the AFMIS terminals present in the line ministries/agencies. Over the past year upwards of 25 ministerial units have been provided access, and the goal according to treasury management is for all

ministries to be granted real-time access by year's-end. This would represent a major step forward towards more time-effective and transparent processing of budgetary approval actions.

At the same time the lack of progress in implementation of a number of critical complementary Free-Balance Modules – including budget preparation/tracking, and asset management, is also hampering efficient integration of budget execution processes. In this regard operationalization and eventual rollout of the budget planning module (which has been under discussion for some time but whose introduction is still not subject to a concrete timeframe), would eliminate the need for manual transcription of budgetary planning/tracking information for AFMIS entry purposes at the line ministry level and within the MOF. However, the implementation of the Free Balance budget module could theoretically require significant amounts of technical/training assistance and entail significant financial commitments. It would also, in all probability, require a lengthy transition and learning by doing process for those line ministries currently using other budget planning and tracking software. Given these factors, it would be advisable to perform a thorough assessment of the available alternatives for promoting more effective automated integration of budget planning and tracking data with the AFMIS system.

The finalization/rollout of the asset management module could prove extremely important from the perspective of facilitating more effective planning of operating expense needs and therefore more effective financial and procurement management plans. This in turn would allow for more transparent and accurate/time-effective budgetary allocation and allotment plans to be developed and implemented through MOF/Treasury. It would of course also facilitate a much more accurate and comprehensive macro-level picture of the physical asset base of the public sector, which would in turn facilitate more efficient and transparent budgetary allocation decisions to be made cross-sectorally and cross-regionally over time. This again reflects the critical role which effective “interfacing” between budget planning and execution activities can play in driving sound budget management outcomes.

There are other vexing budget “interfacing” issues which are frustrating efficient budget allotment processes at the moment. Two of these are effectively “external” to the budget execution policies/practices of the executive branch. In this regard the consistently late approval of the budget by the Parliament (often two months or more into the fiscal year), and the significant revamping of the budget which goes on during this period within the executive branch and between the executive and legislative branches, creates a significant early drag on budgetary allotments and expenditures. And in combination with the current March/February Fiscal Year Cycle, this creates an even greater drag on development expenditures, since it artificially forces a greater fraction of construction expenditures back towards the less climactically hospitable winter months. While this may be addressed to some extent by the imminent changes to the GIROA fiscal year (FY 1392 is intended to begin on or about 21 December), the problems of late budget approval may continue to be a drag on budget execution.

An additional regulatory rigidity which impairs time-effective budget expenditure is the rigid tying of allotments to signed contracts for development budget expenditures. For new contracts, this significantly complicates the initial allotment process and effectively delays project start-up. Moreover donor/GIROA coordination issues also appear to play a significant role in hampering early ramp-up of fiscal year allotments/expenditures. Frequently it appears that donor commitments for development expenditure purposes (i.e. so-called non-discretionary development expenditures) are made very late in the prior fiscal year. This in turn hampers effective corollary project planning activities, as well as complicating the accurate and time-effective development of related financial and procurement plans.

Each of these phenomena appear in turn to be linked to a more fundamental budgetary “interfacing” issue: The lacunae in effective and transparent sectoral planning of development expenditure priorities between line ministries/units and major donors. In this regard an almost universal observation among GIROA counterparts at the MOF and line ministry/agency level was that donor coordination was “one-off” in nature involving coordination meetings with individual donors. In part as a result it had proven very difficult to develop a meaningful sector-wide investment planning mechanism/approach; and there remained a general sense that donors in general continued to minimize the transmission of advanced information about their project investment plans in a manner designed to effectively minimize GIROA a-priori engagement in resource allocation decisions/processes.

This in turn feeds back into the virtual absence of coordination between on and off-budget expenditures which has become an endemic feature of the Afghan budget process. Enhancing this coordination is presumably of fundamental importance not only from the perspective of improving the rationality/impact of budgetary allocation decisions; but also of permitting the type of sound operational planning that will facilitate efficient and time-effective budget allotment processes.

Moreover, there appear to be core institutional capacity issues which are limiting line ministry/agency units at the national and provincial levels from promoting efficient and time-effective budgetary allotment processes. Technical and managerial capacity to drive crisp and well-formulated project design and implementation plans still seems very limited at the national and particularly the sub-national levels. This in turn creates major rigidities in designing accurate and appropriately prioritized expenditure plans that in turn would feed into a more transparent and efficient budget allotment planning process.

Finally, the virtually total absence of cost/benefit analysis and cost/efficiency analysis activities within the MOF, MOED, and the line ministries/units denies the development budget planning process an essential discipline and transparency-inducing influence. Were cost-benefit and cost-efficiency principles applied at the sectoral level over time, this would in turn begin to introduce greater order and clarity and reduce the scope for opaque discretionary development budget allocation decisions; which in turn obscure financial and procurement planning processes and hamper efficient and time-effective allotment processes. In a similar sense, the absence of any type of objective needs-based indicators for helping transparently ration the allocation of development expenditure transfers at the sub-national level creates a ‘discretionary’ budget allocation environment which indirectly but powerfully limits capacity to efficiently and time-effectively map out and manage budget allotment processes. Taken together, the net impact of these policy/regulatory and “mechanical” rigidities in the budget planning and management frameworks is to significantly complicate and extend in time budgetary allocation and allotment processes.

INTERNAL BUDGET CONTROL PROCESSES

As noted earlier the GIROA has made significant progress in putting an overarching legal/regulatory framework in place broadly based on World Bank procurement standards/guidelines. In addition major institution-building and training/outreach efforts have been launched through the MOF and within major line ministries to build basic procurement compliance capacity, largely again through the utilization of embedded donor-financed advisory services. However it appears that there remains a lacunae in the development of detailed manualized procedures which would lay out with clarity operational steps to be followed across all major types of procurement actions. This would prove very helpful in terms of avoiding uncertainties/irregularities which may otherwise arise in relation to specific procurement actions, and could also facilitate more effective training activities for procurement officers. Thus, for instance, the introduction of greater procedural clarity into the actual application of “shopping”

procedures for small-scale procurements could be very helpful in avoiding issues of substance or even simply appearance in relation to the competitiveness characterizing such actions.

At the same time it does appear that the low ceiling for “shopping” actions – approximately \$10,000 currently at the national and sub-national levels - is creating significant rigidities in procurement processes for medium-sized/regularized commodity procurements that are subject to highly structured committee-based bid evaluation processes which take two months or more to carry out. This has reportedly significantly complicated the time-effective procurement of commodities at sub-national levels for operating expense purchases; and appears to impose a significant institutional burden overall on the time-effectiveness and bureaucratic resource-intensiveness of small-to-medium-scale acquisition processes. Having said that, there does appear to be considerable anecdotal information indicating that the rigor characterizing committee-based evaluation/selection processes is not infrequently subject to political influence at both the provincial and the line ministry level.

This provides some indication that the committee process itself is not necessarily insulating decisions – smaller or larger-end - from these influences. Moreover at the provincial level all “shopping” procurements between \$3,000 and \$10,000 are undertaken under the direct guidance/supervision of the provincial governor’s office; which creates additional potential institutional ambiguities. In this regard the absence of a truly independent administrative appeals process effectively limits recourse in such cases. Moreover, the aforementioned peculiarity in bid advertising procedures (a one-day newspaper advertisement/action) potentially limits informational outreach on procurement actions, within the context of current constraints on e-procurement access in rural areas. Finally, additional training in procurement guidelines and in manualized procedures continues to be a priority, across the line ministries and also most particularly at sub-national levels of government.

In the M&E area, while considerable progress has been made in developing the organizational infrastructure for professionalized M&E processes in MOF and major line ministries/agencies, and major training/outreach progress appears to be underway, there do remain important, if relatively nuanced, areas of required policy and institution-building improvement. It does appear that the GIROA is still at an understandably nascent stage in tying M&E plans in a rigorous manner to (1) ministerial operational plans, and (2) program impact indicators. With regard to the latter a key issue is that program-based indicators in general appear to be deficiently defined in terms of final results, or outcome definitions and targets; and this is having a spillover effect in limiting the capacity of M&E officers to efficiently establish and track relevant and measurable performance outcomes.²

In addition the capacity of centralized M&E teams to move out to field offices and both train local staff and oversee M&E information gathering and review activities appears to be constrained at times by budgetary availability. This impacts not only capacity to gather and effectively assess critically important data on project performance, but also to further build up limited sub-national institutional capacity in the M&E area. Finally, while it does appear that in major line ministries progress is being made in developing direct reporting lines between M&E Units and Ministry leadership, it (understandably) appears to be the case that overall the results of M&E review and oversight activities continue to play a somewhat peripheral role in budget allocation and management processes. Presumably a key aspect of changing this will lie in concretizing the results indicators being tracked within M&E Programs; and then tying these in a more direct way to the calculation of annual budgetary allocation needs being developed under program budget planning efforts, by ensuring that indicators are directly linked to program budget planning submissions and reviews.

² This was underscored as a major constraint by the MOF M&E outreach team.

Accelerated progress in the internal audit area is critical to enhanced budget transparency and dramatically tightening the linkage between budget expenditures and service delivery. As noted earlier the almost exclusive emphasis of current audit activity is transaction-audit based. There is virtually no focus on more focused financial audits, nor on operational/ performance- based audits. Narrowly-defined compliance auditing is unlikely to be sufficient to effectively promote budgetary transparency and contractor performance accountability. In addition it will not facilitate the type of on-the-job training required to create an effective cadre of IA experts at the line ministry and provincial directorate levels.

Moreover the development of risk-based annual audit plans appears to be at a very nascent stage of development; although some initial training programs in risk-based audit planning have been delivered in more advanced line ministries (e.g. MOE). Again while the institutional profile of IA units in some major line ministries/agencies appears to have risen, continued uncertainty regarding the role/responsibilities of IA Offices vis-à-vis the CAO appears to represent an ongoing source of institutional uncertainty regarding the guidance that IA Units are receiving in relation to transforming their IA strategy and approaches.

In the HR sphere major and truly impressive progress has been achieved towards centralization of personnel files and related “cleansing” of payroll records, as well as the development of organized P&G systems and performance evaluation processes in major line ministries/agencies. At the same time, significant additional progress needs to be achieved in order to cement or “institutionalize” a new accountability-based pay and performance scheme.

Moreover comprehensive and integrated HR training game-plans have yet to be put in place at the ministry level; much less at the provincial line directorate level (where human resource capacity is clearly the most in need of upgrading). Even in the larger/more institutionally advanced ministries it appears that integrated and effectively-prioritized training plans do not yet exist. Moreover there is little by the way of integrated planning of donor and GIROA-supported training priorities and programs going on at the moment – even though senior technical and middle-management positions within many ministries appear to be dominated by embedded donor-financed staff.

Given the mammoth additional institutional budget management burden prospectively associated with the effective planning and oversight of the envisaged increased level of donor on-budget resources, it is critically important that this type of integrated sector-wide training program coordination process be more effectively framed. Nor has an effective HR sustainability strategy be developed to address the generic issue referenced above: that a plethora of major program planning and implementation activities across major line ministries and within central ministries (MOF/MOE) and related training activities are carried out by embedded donor-supported staff. In particular the data base centralization and cleansing process has not yet been robustly implemented at the provincial and local levels, nor have e-attendance mechanisms been widely introduced at the national and sub-national levels.

BUDGET EXECUTION REFORM - PRIORITIZED RESPONSE OPPORTUNITIES/SUPPORT STRATEGY

The analysis presented above of the budget execution policy/regulatory framework and related institutional architecture underscores the magnitude of policy and institutional reform progress that has been made over the past several years towards the development of a more efficient and transparent budget management and recording system. At the same time, the analysis provides an equally clear picture of the range of key areas where additional policy/regulatory reform and/or institution-building

progress will be required if the budget execution system is to meet better practice-compliant budget transparency and time-effectiveness standards, and to successfully attract/convince major donors to put a larger fraction of their development resources for Afghanistan on-budget. In the analysis which follows, we highlight and prioritize the most critical budget management reform and related institutional capacity-building areas related to the attainment of this goal. This in turn should help illuminate future assistance discussions in the public financial management area.

CORE BUDGET EXECUTION PROCESS REFORM STRATEGY

The donor community can play an effective role in promoting critical budget management-related policy/regulatory reforms which could significantly enhance the time-effectiveness and transparency of core budget execution procedures/processes. This will entail effective policy dialogue with senior level MOF and line ministry counterparts, as well as coordinated dialogue/ action among all key donors (e.g. World Bank, IMF, USAID, DFID, DANIDA) engaged in promoting additional reforms in these areas. Given the magnified post-Tokyo Summit focus on moving a higher proportion of donor resources on-budget as quickly as possible (with a reported near-term target of 50%), reforms across a number of critical areas will be required to facilitate compliance with this objective. Forward movement in these areas could be effectively articulated/monitored within the context of time-framed project/program-level agreements to transfer additional donor funding on-budget; in accordance with bench-marked progress in critical budget execution policy/regulatory and institutional realignment areas. This could prove extremely important in terms of building the political support/momentum required to follow-through on policy and institutional reforms that by their very nature touch on sensitive budgetary transparency and probity issues.

Driving accelerated reform in key budget management areas will also require the allocation of targeted technical/training and (where relevant) corollary financial resources in a manner which effectively supports progressive institutional actors in GIROA central budget control agencies, major line ministries/agencies and at the provincial directorate level, in “sponsoring” and effectively institutionalizing advanced budget execution processes. The most critical reform and related technical/training support areas from a budget efficiency/transparency, time-effectiveness and accountability perspective are enumerated below:

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Further Streamline Budgetary Approval Processes: As noted earlier despite recent progress, the budget allotment process continues to be characterized by duplicative review/approval processes within the MOF; and can require up to 14 to 16 signatures for approval purposes. The payment authorization process, although less bureaucracy-intensive, can require 7-9 signatures between the time the 1st request form is prepared within a given line ministry until it is approved for disbursement by MOF/SDU. These processes can each take up to 3 weeks. There reportedly remain serious issues in many line ministries with delegation of signatory authority, which can significantly delay approval actions as well. Further streamlining of document flow/approval processes in these areas could potentially save 1 ½ - 2 weeks in processing time per budgetary approval action.

In addition, consideration should be given to moving away over time from the strict requirement that budget allotment requests for new projects be strictly tied to the finalization of contracts with project implementers. This requirement as noted earlier can itself significantly delay initial allotment processes required to put financing in place for major new funding programs. Discussion appears to be underway within MOF and some major line ministries of movement towards an annual allotment process which would eliminate this potential rigidity and allow for more streamlined and predictable allotment and related financial planning. In cases where expected project start-up timeframes extend out significantly, re-allotments can be executed under the aegis of current mid-year budget review process. Alternatively,

to ensure closer parliamentary involvement in allotment modifications and reduce executive budget modifications without parliamentary approvals, modifications could be done on a quarterly basis by a duly authorized parliamentary committee by request of GIROA/MOF.

Promote More Time-effective and Transparent Budget Allocation/Allotment Processes: As noted earlier the development of annual finance and procurement plans are a critical new tool introduced this past year to bring greater rigor, predictability and transparency to the budget allocation/allotment system. As is to be expected, initial implementation has been fragile in terms of comprehensiveness and the accuracy of information submitted. Indications from a number of line ministries and relevant MOF staff is that much additional progress needs to be made at the line ministry/agency and provincial directorate levels in the provision of unified and accurately forecast financial and procurement plans in order to significantly enhance the transparency and predictability of budget allocation and allotment processes; and to facilitate more effective Treasury cash management policies. This will in turn help avoid the anecdotally reported delays which appear to periodically occur between allotment approval and cash disbursements hitting the appropriate DAB central or provincial level accounts.

In addition, intensified ministerial commitment to the development of comprehensive and detailed operational plans is also important for purposes of introducing greater order and transparency into budget allocation and allotment processes; and decreasing the reliance on the type of *ad hoc* budgetary decision-making which contributes to the “piling-up” of un-committed development expenditure funds during the early stages of the fiscal year. These reforms could be supported through targeted technical/training support within the MOF and on a pilot basis in key line ministries/agencies. This could also entail support in pilot Mustofiats and provincial line directorates (with regard to budgetary approvals for sub-nationally sponsored pilot development projects) and for local operating expenses.

Promote Integrated Automation of Budgetary Execution Processes: The lack of full and effective integration of AFMIS at the line ministry level is of course delaying budget allotment (most particularly) and payment authorization requests from the line ministries/agencies. In this regard pushing towards real-time integration/access to AFMIS across all line ministries will help further improve the time-efficiency of budgetary execution actions and enhance development fund expenditure rates. In addition, the adoption of a budget module compatible with Free Balance and possibly with automated budget systems currently in use in line ministries, and its longer-term integration within at least the major line ministries, should further enhance budget processing time-efficiencies. It would achieve this by reducing multiple data entry and manual data consistency cross-checking activities, as budget information and consistency-checks are done directly through entry into the budget module both within the MOF and at the line ministry level.

In addition the development/deployment of the asset management and procurement modules of Free-Balance could significantly enhance the transparency and efficiency of budget management activities. The asset management module could play a major role in facilitating comprehensive and accurate information regarding the physical/project asset base of the public sector, thereby enhancing institutional capacity to engage in effective planning of additional capital projects and develop more accurate O&M expenditure needs estimates, which would feed back into the financial and procurement planning process so critical for efficient and time-effective budget execution processes. The procurement module can help establish a centralized and readily access-able data base on procurement action plans/status which will both create more transparent information about procurement actions and again help facilitate more efficient and time-effective financial and procurement planning and streamlined budget allotment processes. It should be noted in this regard that adoption and application of the Free Balance budget module may be somewhat more problematic, as independent systems are already in use in major line ministries. To

mandate the wholesale abandonment of those systems is to risk significant “transitional” losses in time-effectiveness and processing efficiency, and might prove politically unpalatable as well. Thus, although the application of a budget module is indicated, a thorough and technically detailed assessment of the potential IT system architectures that could permit this functionality to be most effectively achieved should be carried out *a priori*.

In short there would thus appear to be ample opportunity in the near term for a cooperative inter-donor effort to spur additional expeditious progress towards implementation on at least a pilot basis of key critically important AFMIS Modules (procurement, asset management) over the next 1-2 years. The World Bank and the MOF Treasury Department are the critical institutional interlocutors in this area. Overall there would appear to be natural scope for effective engagement with the World Bank and with Treasury to facilitate technical/training and (as needed) financial support for the finalization and roll-out of these modules over the next 2-3 years; including in pilot line ministries/agencies and provincial Mustofiats. What will be required most importantly in this regard is effective political leadership within the MOF and GOA; and effective inter-donor coordination.

Reduce Uncertainty in the Allocation of Development Budget Resources Across Sectors/Regions: The final assignation of own-financed development fund budgetary resources across sectors and provinces is effectively made after the start of the fiscal year; and reflects to a significant degree last minute political “horse-trading” effectively conducted outside the structured context of the program-driven budget allocation process. This appears to create an atmosphere of uncertainty which delays and introduces uncertainty into the financial and procurement planning process, which then in turn complicates/delays initial budget allotment actions and creates challenges for efficient Treasury cash management planning activities. This is in addition to the scope which this practice introduces for discretionary budget allocation decisions which (1) do not necessarily reflect objective expenditure needs-based criteria, and (2) may not be entirely consistent with the implicit program-based budget allocation which is reflected in the budget initially sent to the Parliament (at present the Parliamentary-approved budget does not explicitly prioritize/allocate resources by program). Reigning-in the discretionary allocation of own-financed development budget resources such that these are more transparently allocated, and in a manner which promotes greater consistency in a-priori planning for related operating expense forecasts, will again facilitate more effective budget allocation/allotment forecasting and cash management activities.

Similarly, the late timing in which the donors and GIROA confer/agree on non-discretionary development expenditure priorities, as noted earlier, significantly complicates and inhibits time-effective and efficient budgetary allotment, financial and procurement planning and cash management activities. This in turn appears to be related to a couple of fundamental inter-institutional budgetary coordination issues: First, there appears as briefly referenced above to be limited focus either among the donors or at the MOF/line ministry level on establishment of a well-organized and operationally-relevant sector-level coordination process on development funding priorities between the donors and lead ministries. Nor does there appear to be such a focus at the regional/provincial level.

In this regard a number of relevant budget management counterparts at the MOF sector level and within the line ministries/agencies have indicated that information on donor project priorities/plans is shared in a manner and within timeframes which are less than effectively conducive to sound discussion and related program and budgetary planning processes. This in turn creates difficulties from an operational planning and financial and procurement plan development perspective at the ministry and line directorate level. Moreover behind this budget coordination rigidity issue in a more fundamental sense is the entire question of the absence of effective de-facto coordination between the GIROA budget and the huge volume of off-budget expenditures being financed by the international community.

The lack of integrated planning of off and on-budget priorities is clearly hampering the capacity of the GIROA line ministries and provincial directorates to rationally prioritize and program their own development and related operating expense resources, and to develop well-organized and time-effective financial and procurement plans. This fragmented budget planning process is thus grossly suboptimal from a rational budget resource planning perspective; as well as from an efficient and cost-effective budget management viewpoint. Resolving these issues will prove of critical importance from the perspective of creating a smooth budget planning and control framework for time-effectively transitioning a large additional volume of donor expenditures on-budget. It will also help ensure that the joint allocation of off and on-budget expenditures by sector/program and by province reflects a sound prioritization process which more accurately reflects critical socioeconomic needs of the population.

Another critical issue driving budgetary allocation uncertainty is the aforementioned ongoing absence of expenditure norms at the sector level which reflect objectively-defined socioeconomic needs indicators. While information in this area still needs to be improved, it is difficult to justify a full decade into the transition process the very limited allocative focus on objectively-defined need proxies in critically important areas such as health, education, and sanitation. The utilization of these indicators is reportedly being considered on a pilot basis in key sectors under the guidance of the MOF Provincial Coordination Unit. Accelerated progress in this area could help significantly reduce the budgetary uncertainties which hamper effective allocation/allotment processes early in the fiscal year, as well of course as promoting a more rational overall allocation of budget flows in relation to socioeconomic expenditure needs. The donor community could in this regard provide targeted technical support to facilitate pilot application of sound needs-based expenditure norms at the sector-level to facilitate greater rationality and predictability of the budget process; and to correspondingly promote more transparent and time-effective financial and procurement planning and budgetary allotment processes.

Implementation of Improved Financial/Procurement and Operational Plans: It is critically important to build upon the path-breaking progress recent achieved in mandating GIROA-wide development of annual financial and procurement plans as a critical component of an enhanced budgetary allotment and treasury cash management system. However this process is still at a nascent stage of development. Similarly the development of reasonably detailed and appropriately prioritized operational plans is critical for both sound budget planning and budget tracking/reporting purposes. Additional targeted technical/training support at the line ministry/agency and provincial directorate level could prove critical in supporting basic donor and GIROA goals of improved expenditure rates and greater budgetary transparency/ accountability.

It would also introduce a type of budget prioritization and management discipline which would itself help accelerate the process of better coordinating off and on-budget donor expenditure programs and gradually merging them within the GIROA annual budget process. This would obviously have to be introduced in a gradual manner, but given that Afghanistan is now a decade into the fiscal transition process it is presumably time to initiate reform steps in this direction. This could be done in a manner which reinforces the momentum behind and impact of the pilot provincial program budgeting reforms; by promoting at least pre-feasibility studies for subsequent rounds of pilot projects to be financed under these programs.

Improved Project Design & Operational Management: As noted earlier both GIROA and donor officials consistently pointed to weaknesses in basic project design and oversight capacity as a critically important constraint for mapping out and effectively executing sound budget management plans; and that that this most particularly was associated with sluggish project start-ups and expenditure rates during the early stages of project implementation. Targeted technical/training support in selected major line

ministries/agencies would thus appear to be a significant priority if the placement on-budget of major additional donor resources is to be carried out in a manner which does not “clog-up” the budget execution system.

Development of Basic Cost/Benefit and Cost-Efficiency Analysis Capacity: As discussed above Afghanistan is now a full decade into the fiscal transition process; and yet it appears that little by way of financial and economic pre-feasibility or feasibility analysis is being effectively carried out on own-financed development projects. Nor is there any capacity in this area for helping ground-truth the project priorities proposed by donors. At this point the core selection litmus-test appears to be a consistency check undertaken by MOE and double-checked by MOF for consistency of project proposals against broadly defined ANDS priorities. This is extremely important, but does not provide rigorous criteria for understanding/ranking the relative socio-economic returns of alternative project initiatives.

Clearly given the volume of resources likely to be shifted on-budget in the coming years, it is critically important that at least some basic pre-feasibility analysis capacity be developed and applied to discipline the project selection process. Given the overwhelming nature of the socioeconomic development needs in the major sectoral areas in which investment projects are undertaken, it is likely in the near-term that the analytical focus would be predominantly on cost-efficiency analysis (particularly in areas like health and education), with cost/benefit techniques being more directly relevant in most instances to physical infrastructure projects. The key point here is that a beginning needs to be made in developing and applying standardized selection criteria for major investment projects, if the GIROA and their donor partners are to ensure that the upcoming multi-year tranche of donor resources prospectively targeted for on-budget are to be utilized in a manner which dramatically improves socioeconomic conditions and sustainably enhances social and political stability. This represents a critical interface between the budget planning and execution areas; since sound project analysis work also facilitates more effective nuts-and-bolts operational planning (referenced above) and lays the groundwork for more disciplined and time effective budget allotment and oversight processes. Technical/training support in these areas is a critical priority within major line ministries/agencies, and of course at the provincial directorate and Provincial Development Committee level as well, as development expenditure processes become more decentralized over time.

INTERNAL BUDGET CONTROL REFORM STRATEGY

Accelerated implementation of a number of key ancillary budget control reforms could also prove critical to creating a more transparent and accountable budget execution system. Top reform priorities in these areas are concisely outlined below:

Accelerated introduction of more rigorous procedural and implementation frameworks and appeals processes for public procurement: The finalization and implementation of detailed and manualized procedures for procurement actions within key line ministries/agencies; and the related detailing of more systemic procedures for the selection of “shopping” based procurements (while increasing the ceiling for their application) can have an important impact on the transparency and rigor characterizing procurement processes. These reforms should extend down to the provincial level as well; as local oversight of procurement actions will become more important with the pending focus on greater decentralization of development expenditure planning (initiated through the provincial program budgeting pilots). In addition the creation over the longer-term of a more independent administrative appeals framework for procurement actions could prove important from a budgetary transparency/accountability perspective.

In this regard the donor community could usefully provide targeted technical/training support to promote full operationalization of detailed and manualized procedures for procurement actions, and smoothed implementation of bid advertisement, evaluation/selection and appeals procedures for different major procurement categories. This could be carried out in key line ministries/agencies (and related provincial directorates) whose budgetary resources are expected to swell as a result of the transfer of significant amounts of donor resources on-budget. In the appeals area, the support would be provided to the MOF-headed appeals unit or to an independent procurement appeals body should this be formed/established.

Improved Design/Implementation of M&E Plans: Significant recent progress has been made within MOF and (with their support) in major line ministries/agencies in the development of coherent and well-organized M&E Plans and tracking systems. This could be significantly further improved through targeted technical/training support at the line ministry and provincial directorate levels geared towards (1) significantly improving the concrete goal-focused nature of the ultimate performance targets being tracked (thereby complementing support being provided in the program budgeting area by focusing intensively on better defining programmatic outcomes in key sectoral areas); and improving data gathering and collation processes and establishing more streamlined and effective feedback M&E loops with program offices (while maintaining independent annualized reporting channels with line management).

Accelerated implementation of Risk-Based Internal Audit Planning and Procedural Frameworks: Initial reform steps have been taken to institutionalize IA units in major line ministries and build basic IA operational capacity. However meaningful risk-based audit plans are not in place in major line ministries/units and it appears that narrowly-defined transaction-based compliance audits are the operating norm in virtually all line ministries/agencies. This is not terribly surprising/unexpected at this stage of development of the budget execution system in Afghanistan. However if the donors are to place significant additional funding on-budget under local control, then more ambitious progress towards adoption of risk-based annual IA plans and at least pilot introduction of more focused financial and operational audit activities becomes a clear and important priority. Overall, it appears that intensive additional institution-building progress and further visible bureaucratic/ political focus on the importance of at least basic risk management-focused audit activities within major line ministries will be required in order for IA functions to be carried out in a manner which impact in a tangible way on budgetary transparency and efficiency.

In this regard the donor community should consider the provision of targeted technical/training support to reinforce the effective work which U.S. Treasury has initiated through its outreach/training support program with the MOF IA Unit and which a number of donors have provided in some of the larger central ministry/agency units. This could take the form of targeted technical support and related OJT and formal training modules in selected major line ministries and agencies, and at the provincial directorate level. These should focus primarily on (1) development of basic risk-based internal audit plans; and (2) effective pilot application of risk-based audit approaches/ techniques in the conduct of financial and operational audits.

Completion of Centralized Personnel Registration and Payroll Record “Cleansing” Process: Impressive progress has been made in cleaning up and systematizing the personnel data base system the GIROA and effectively addressing the ghost employee issue. At the same time it is important that the massive ongoing personnel database centralization and payroll record cleansing process continue and be extended down across all line units to the provincial and local levels; and that phased implementation of

e-attendance based mechanisms be comprehensively introduced at the national level; and then in sub-national units. From a budgetary probity and efficiency perspective it is important that the process be brought to effective completion over the next 2-3 years with a particular focus on verification of the employment status of all staff and related cross-checking of personnel files against payroll records at the sub-national level.

This will need for the foreseeable future need to be done on a ministry-by-ministry basis; since it appears that movement towards a unified automated payroll system is not likely to prove feasible in the near-to-medium term. In this regard the Free-Balance payroll module reportedly lacks the capacity to handle the volume of records required for this purpose in Afghanistan, and so does not seem a relevant option at the moment. In addition, accelerated introduction of e-attendance systems (including at the local level) in major line ministries/agencies will be important for purposes of ensuring the integrity of the revamped human resource management system, and enhancing the accountability of public servants in the eyes of the Afghan population.

Systemic Implementation of a Civil Service Transition/Sustainability Plan: The aforementioned dominant role played by donor-financed line staff in key technical and mid-management positions across an array of line ministries, and within the MOF itself, is widely recognized as a fundamental constraint on sustainable public service provision capacity over the longer-term. This clearly underscores the importance of development and implementation of a comprehensive game-plan to ensure that the budget management and indeed the entire public service provision system does not suffer severe dislocation once the transition to a civil service-based pay scale for all line staff is completed. Thus the implementation of an effective and sustainable strategy for integrating embedded staff specialists within the permanent civil service is an absolute priority from a budget planning/management as well as from a much broader public sector legitimacy and governance perspective.

Some initial pilot efforts are underway in this direction (i.e. the World Bank-supported CBR Program, which is “topping off” salaries of donor-supported specialists to upper-end civil service pay grade levels during a defined transition period to facilitate their eventual transition to civil service status). It should be noted in this regard that down the road “topping-off”-type compensation programs may create an expectational issue by creating “hard” compensation ceilings for senior technical and managerial specialists who are already at the upper-end of their pay-scales in senior positions. However this is presumably an issue which could be addressed over the longer-term though overall adjustments to the civil service pay system.

Overall it is clearly critical that a comprehensive game-plan in this area be developed and agreed upon with the major donors. This will likely require augmented financial support in order to prevent the erosion of the human capital resource base which the GIROA and donor community have worked together so assiduously to develop over the past decade; as well as to further expanding nascent training efforts to the sub-national level (as further detailed below).

Development of Viable Integrated Human Resource Training Plans/Programs: The absence of a comprehensive and well-integrated HR training plan appears to represent a clear and pressing need in major line ministries/agencies. This in turn largely reflects the fragmented nature of the human resource development process as impacted by the support programs of a plethora of different donor agencies. Given the importance of this area from an effective budget planning/control and effective and accountable public service delivery perspective, USAID should consider a targeted technical support initiative to “jump start” development/ implementation of a coherent medium-term training strategy and program at the pilot line ministry/agency level. This would in turn entail the coordinated utilization of both on-budget and donor-funded off-budget resources in support of priority HR institution-building

needs at the pilot ministry and related line directorate level, as well as interaction with the GIROA Civil Service Commission and/or the Civil Service Institute, which hold the legal mandates for training of civil servants.

PROSPECTIVE INSTITUTIONAL FOCUS OF DONOR SUPPORT EFFORTS

For most of the areas referenced above the critical locus of institution-building support would be within pilot line ministries/agencies and their corresponding provincial directorates. In the budget administration process and MIS application areas; MOF and provincial Mustofiats would be a significant focus of support as well. In the capital budgeting area the Provincial Development Committees would be a clear potential target of institution-building support. In determining the how/where to best to focus support at an inter-institutional level, the donor community should take into account three principal allocative factors: (1) the importance of a given sector from an efficient public resource management perspective; (2) the magnitude of pre-existing effective donor institutional presence in a given sector/reform area; (3) GIROA readiness/interest/ commitment to move forward to accelerate reforms in a given reform area. Based on this assessment, an effective determination can then make as to where to optimally focus relevant policy/regulatory reform and/or related institution-building support programs, both in terms of budget execution reform area and related sectoral targets of opportunity.

In addition, the expressed readiness of supported institutional actors to engage in the difficult institutional reform/re-shaping actions required to achieve additional progress in core budget execution areas must be incorporated as a critically important factor in determining where/how to allocate donor support resources. This is particularly important given the demonstration effect impact (positive or negative) that the success of a fresh round of budget execution support efforts in these areas will have on subsequent dissemination progress at the national and sub-national levels. In this regard the development of MOU-type agreements that lay out shared programmatic commitments between a given donor and the administrative unit receiving support could represent an effective modality for helping “self-select” reformist institutions; and for helping to better organize and gauge effective progress under specific budget execution reform/institutional strengthening efforts.

In principal it would of course make sense to focus on supporting reforms in institutional/sectoral areas where improved budget execution performance is likely to have the strongest impact on socio-economic welfare improvements and enhanced legitimization of the GIROA’s public service delivery capacity in the eyes of the public (i.e. education, health care, sanitation). At the same time, given patterns for pre-existing donor presence and/or differential commitment to reform across line ministries and provinces, it could make sense to in some instances implement pilot reform support efforts in smaller ministries or less populated provincial areas where the prospects for successful pilot applications may be greater. These are tactical determinations which need to be made at the field level.

In each of these politically sensitive fiscal reform areas it is critical for key donors to jointly work with the MOF and with the Economic Cabinet to map out prospective reform actions and timeframes to which could be tied both technical /training support game-plans (the above-referenced MOU concept); and to consider tying broader financial commitments to move additional funds on-budget to demonstrated progress in key budget execution areas. This would both provide a pragmatic and coordinated fiscal institution-building prioritization framework; as well as providing very direct incentives for forward progress which would promote the shared GIROA/donor goal on moving a significantly greater share of donor resources on-budget within defined timeframes. In their absence, it may prove difficult to overcome the political economy inertia which continues to promote opaque budget execution outcomes at the line ministry and provincial levels.

Under such an approach the donor community would focus on interventions in budget execution policy/technical areas through which a decisive contribution can be made to enhanced budget execution efficiency/transparency; and with partner institutions which are prepared to demonstrate clear commitment to move forward. The MOF would represent an “omnibus” or virtual partner in the development of these support programs at the line ministry/agency level, as would both MOF and IDLG at the sub-national level. In selected technical support areas the MOF might also effectively serve as a co-sponsor and co-organizer of targeted training and technical support activities (e.g. introduction of risk-based audit plans, improved annual M&E plans). It could also prove useful to engage academic/training institutions in the provision of targeted longer-term training in key public finance skill areas which interface budget planning/execution areas (e.g. cost/benefit analysis, program budget analysis, inter-governmental finance); and to arrange with key GOA counterpart institutions (e.g. MOF, MOED) to utilize donor-supported programs in these areas as a mechanism for raising skills of existing staff and as a recruitment source for additional staff.

It is clear that forward movement in virtually any area will require coordinated action with a number of major donors, as there is virtually no budget execution area examined under this study that does not have some degree of pre-existing coverage by other major donors. One key point in this regard is that both the current locus of donor support efforts in most of these areas clearly appears to be at the national rather than the provincial level. In addition the most severe shortfalls in institutional capacity are clearly at the sub-national level. Given these realities, and given the strong institutional interest (embodied in the recently initiated pilot provincial budgeting program) in beginning to decentralize to some degree control over the budgeting and procurement process; strong consideration should be given to focusing intensively on the provision of institution-building technical and training support in key budget execution areas at the sub-national level.

CONCLUSIONS

The budget execution system in Afghanistan has experienced dramatic regulatory and operational improvements over the past several years. A core AFMIS system has been introduced with the MOF/Treasury office and real-time connectivity achieved with line ministries/agencies and provincial Mustofiats. Budgetary allocation/allotment and payment approval processes have been systematized and streamlined. Annual Financial & Procurement Planning Processes have been established and nascent operational plans developed at the line ministry/agency level. As a result of these reforms, execution rates on the operating expenditure side reached approx. 94 % in 1391, while development expenditure rates rose to 52%.

A World Bank procurement guideline-based legal/regulatory framework for public procurement actions has been established, and organized M&E game-plans and annual reporting frameworks established at the line ministry level. Basic IA annual plans are being implemented and transactional audit-based activities carried out for major line ministry/agency units. Embedded donor-financed line staff are guiding the implementation of and providing training outreach support in all of these areas; through centralized MOF outreach units and directly at the line ministry/agency level. In the HR area major progress has been made towards centralizing personnel files and cross-checking these against payroll records in order to effectively “cleanse” the system of ghost employees; and e-attendance systems are being introduced across a number of major line ministries/agencies. Pay & Grading reforms and standardized job evaluation and promotion systems are also being introduced. In short the budget execution system has undergone a compelling transformation over the past half-decade.

At the same time major challenges remain to be overcome if the budget execution system is to meet the budgetary transparency, time-efficiency and accountability standards required to significantly augment public confidence in the sustainable service delivery capacity of the public sector in Afghanistan. Moreover these reforms are critically important if donor policy and/or statutory requirements for placing significant additional amounts of financial resources on-budget are to be met. In this regard although development budget execution rates have risen recently, they still rest at a level which is quite low at a time when the GIROA is expecting at least 50% of all donor resources to be transferred near-term to direct GIROA control. Development budget-related allotment and payment authorization processes still require 2- ½ - 3 weeks on average – a timeframe which can and should be cut considerably.

The budget execution system remains semi-automated with partially duplicative paper-based and electronic data submission/transfer processes continuing in place, in part because of the continued operation of parallel budget processing software systems and because of high data entry error rates. A number of institutional rigidities in the budget allocation process (some “external” and others within GIROA operational control) limit the pace of “startup” budget execution activities early in the fiscal year, while basic shortcomings in institutional capacity limit the GIROA’s capacity to develop the type of financial and procurement plans and operational plans required to promote time-effective and efficient budget execution. In critical budget planning/execution “interface” areas (e.g. project feasibility analysis, project design and operational oversight), limited institutional rigidities and capacity shortfalls have introduced uncertainties and opaqueness into the development budgeting oversight process which is harmful to the pace and transparency of budget execution.

Moreover, institutional weaknesses in the IA and M&E systems limit the GIROA’s ability to promote strong linkages between expenditure patterns and performance outcomes; while significant additional progress remains to be made in finalizing the employment record “cleansing” process, and establishing a comprehensive P&G and related training system that will provide a sustainable institutional basis for effective public service delivery over time. Moreover, comprehensive resolution of the issue of how best to promote a smooth transition of senior donor-financed technical and managerial staff to permanent civil service-financed positions is an urgent priority for purposes of ensuring continuity of GIROA personnel and effective public service provision..

The donor community can play a key role in promoting targeted regulatory/institutional reforms across a number of these critically important budgetary reform areas. These most prominently include promoting rapid finalization/roll out of critical AFMIS budget processing/reporting modules; procedural reforms which further streamline budgetary allotment/payment authorization processes; regulatory reforms which reduce uncertainty in budget allocation/allotment processes; phased-in application of project pre-feasibility/feasibility analysis processes; mandated movement towards risk-based IA approaches; and implementation of a practical approach to transitioning key donor-financed GIROA positions to permanent civil service status/financing. In each of these politically sensitive areas it is critical for key donors to work with the MOF and the GOA overall to map out prospective reform actions and timeframes to which could be tied both technical /training support game-plans and broader financial commitments related to moving additional funds on-budget. This would both provide a pragmatic and coordinated fiscal institution-building prioritization framework; as well as provided very direct incentives for forward progress which would directly promote both the shared GIROA/donor goal on moving a significantly greater share of donor resources on-budget in a defined timeframe.

Donors can also provide critically needed technical and training support which would build institutional capacity and significantly enhance the time-effectiveness, transparency and efficiency of the budget process. Critical areas could include technical/training assistance for (I) accelerated AFMIS rollout and

related budget process streamlining reforms; (2) tightened financial and procurement planning and operational planning processes; (3) improved budget allocation norms at the regional level; (4) improved project analysis capacity and procedures; (5) more transparent and time-effective procurement procedural frameworks and implementation processes/practices in key line ministries/agencies; (6) improved risk-based audit plans annual plans and methodological practices; (7) tighter and more goal-focused M&E plans and oversight processes in key line ministries/agencies; and (8) more comprehensive/integrated and better prioritized HR training programs in key line ministries/agencies.

Given the politically sensitive nature of these critically important fiscal reform areas, it is critical for key donors to jointly work with the MOF and the Economic Cabinet to both map out prioritized and time-framed technical/training game-plans, and to also develop a roadmap of prospective reform actions and timeframes which would help drive the provision of targeted technical /training support. It could also prove important for donors to link commitments to move additional donor funds on-budget with demonstrated regulatory and institutional reform progress in key budget execution areas. This would help promote demonstrated GOA sponsorship of the budget execution reform process. It could also facilitate the establishment of a systemic and well-coordinated fiscal institution-building support network; which could help donors and the GOA effectively monitor progress towards closing key institutional gaps, and determine where/how budget execution-related institution building support resources can best be allocated over time. It would simultaneously effectively address key risk management issues which are currently inhibiting donors from placing a larger percentage of their developmental funding on-budget.

The MOF would represent an “omnibus” or virtual partner in the development of budget execution support efforts at the line ministry/agency level, as would both MOF and IDLG at the sub-national level. In terms of geographic focus, in principle it seems clear that relatively little donor support is being provided to improve budget execution transparency/ efficiency at the sub-national level (e.g. Mustofiats, line directorates, Provincial Development Committees); and this would appear to represent a prime potential focus for impactful institution-building support in key budget execution reform areas moving forward.

APPENDIX A: Budget Process Flow Charts

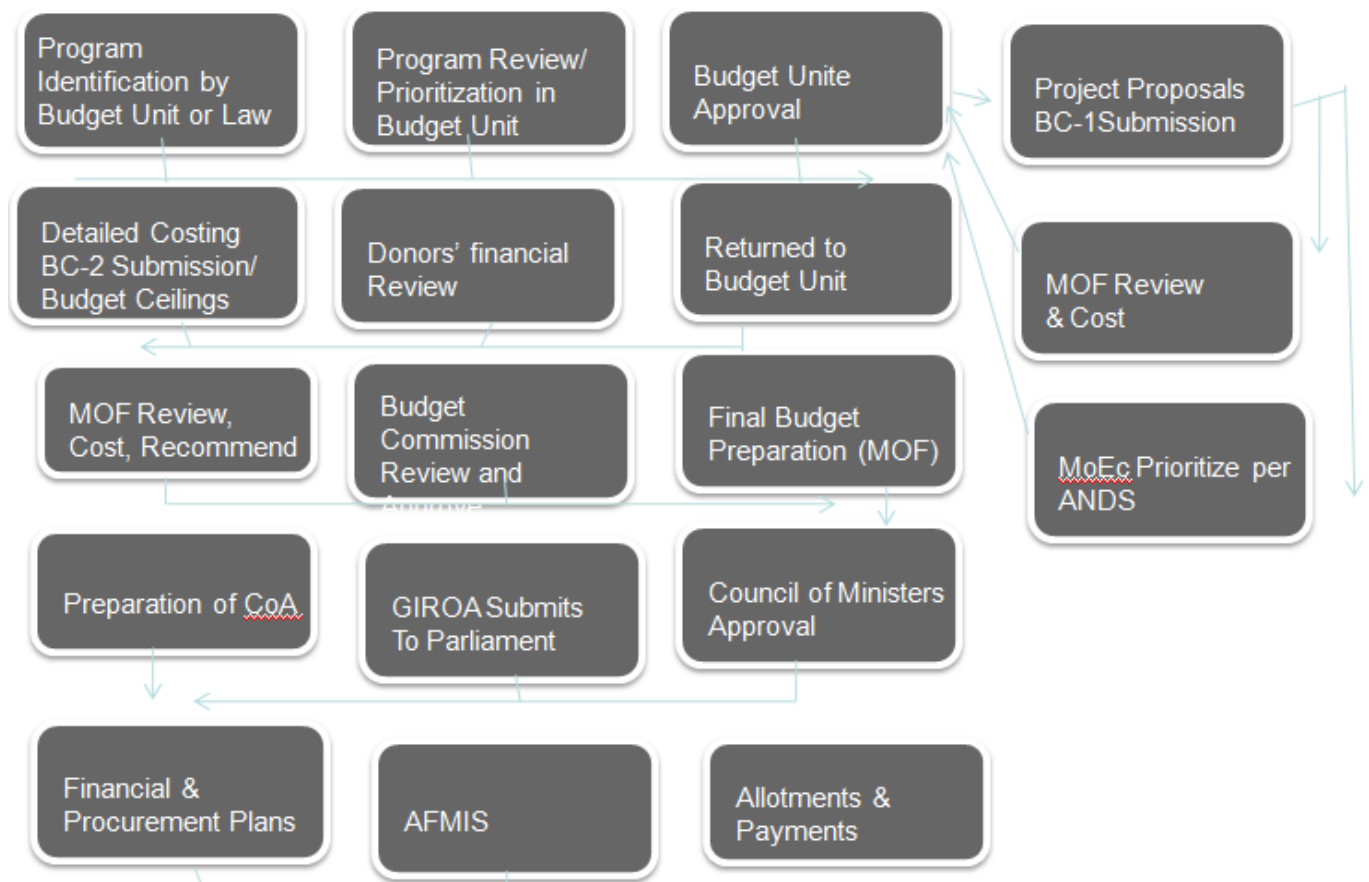


Figure 1: GIROA Budget Development Process

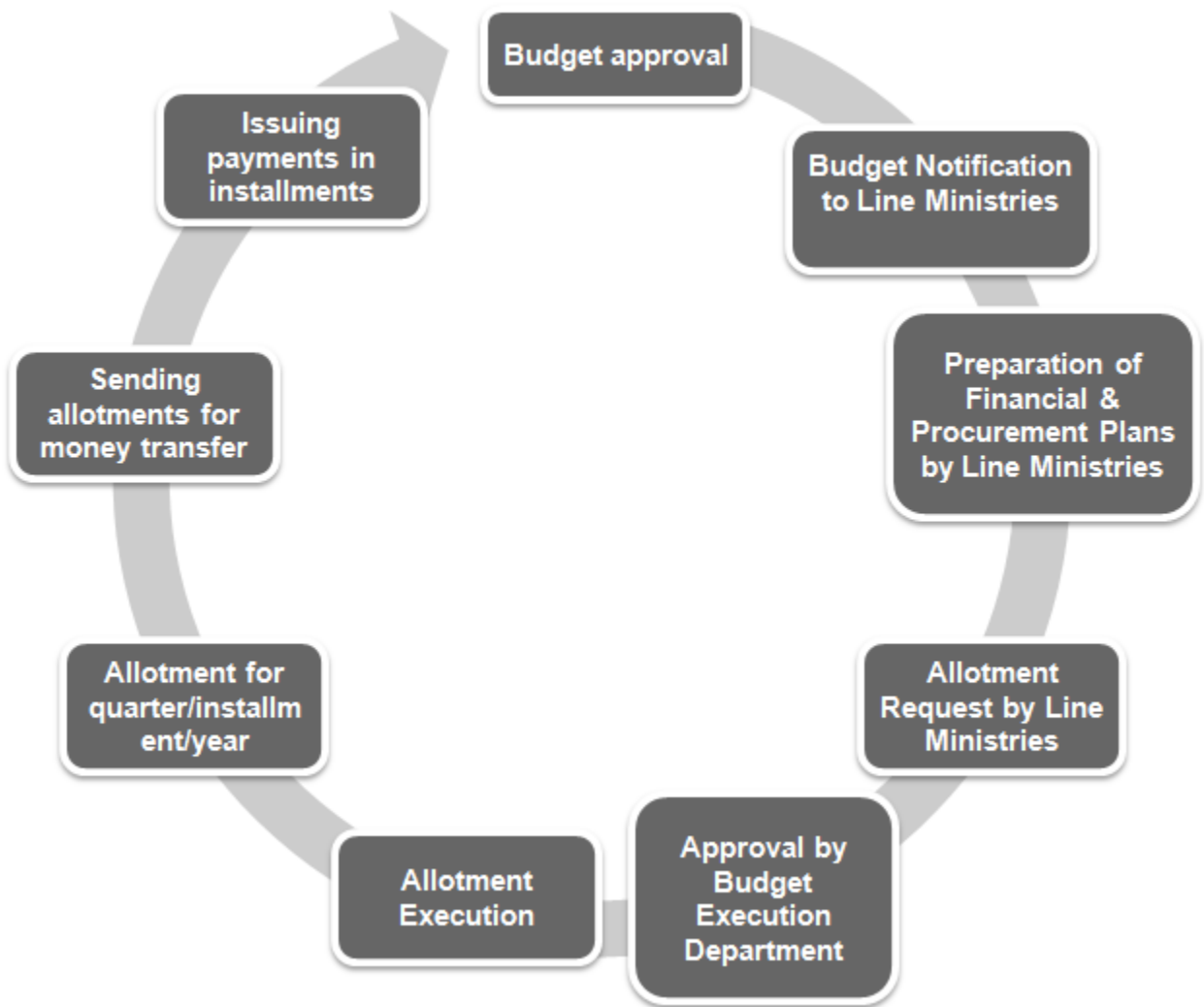


Figure 2: The Budget Execution Cycle

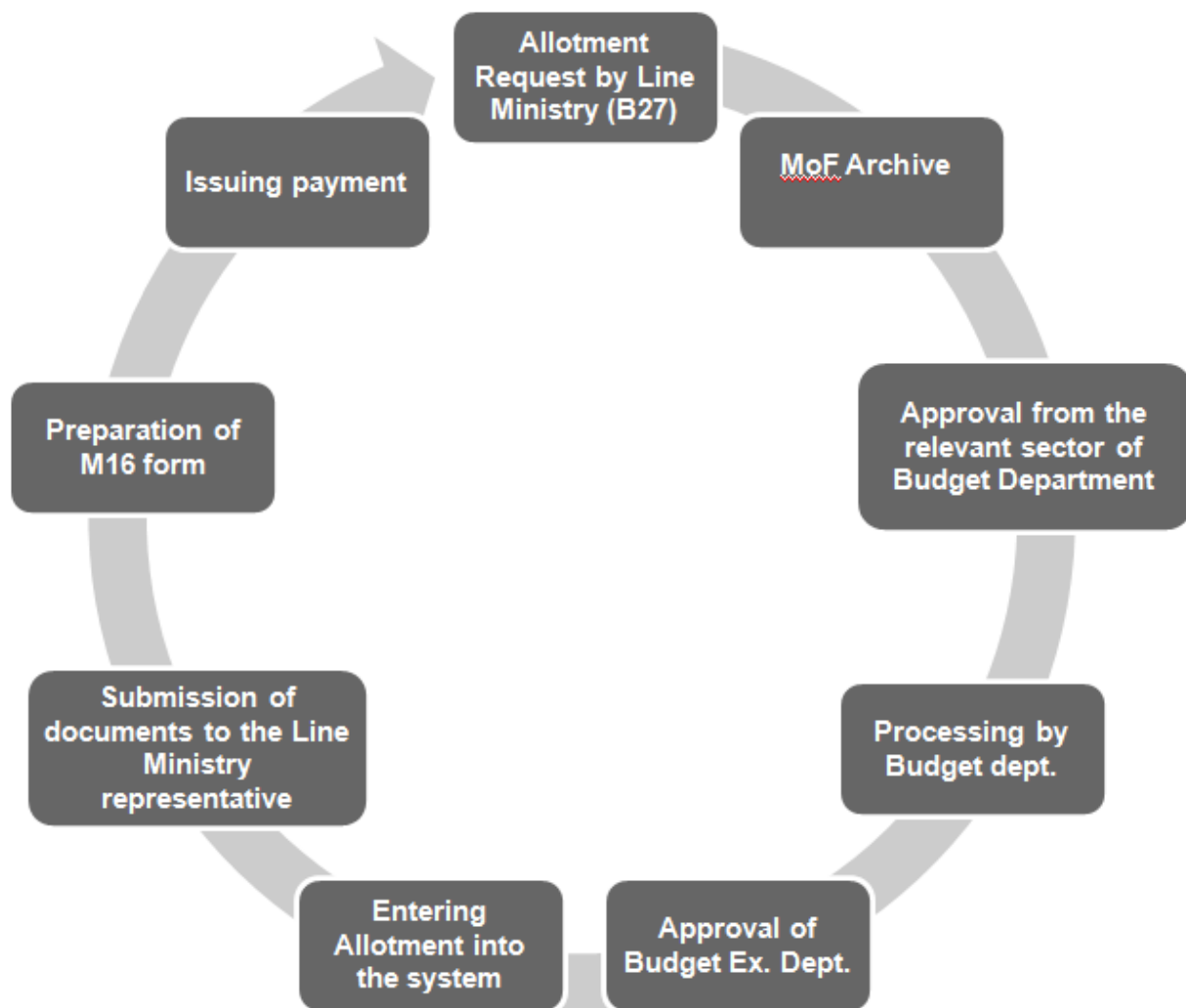


Figure 3: Budget Allotment Execution Cycle

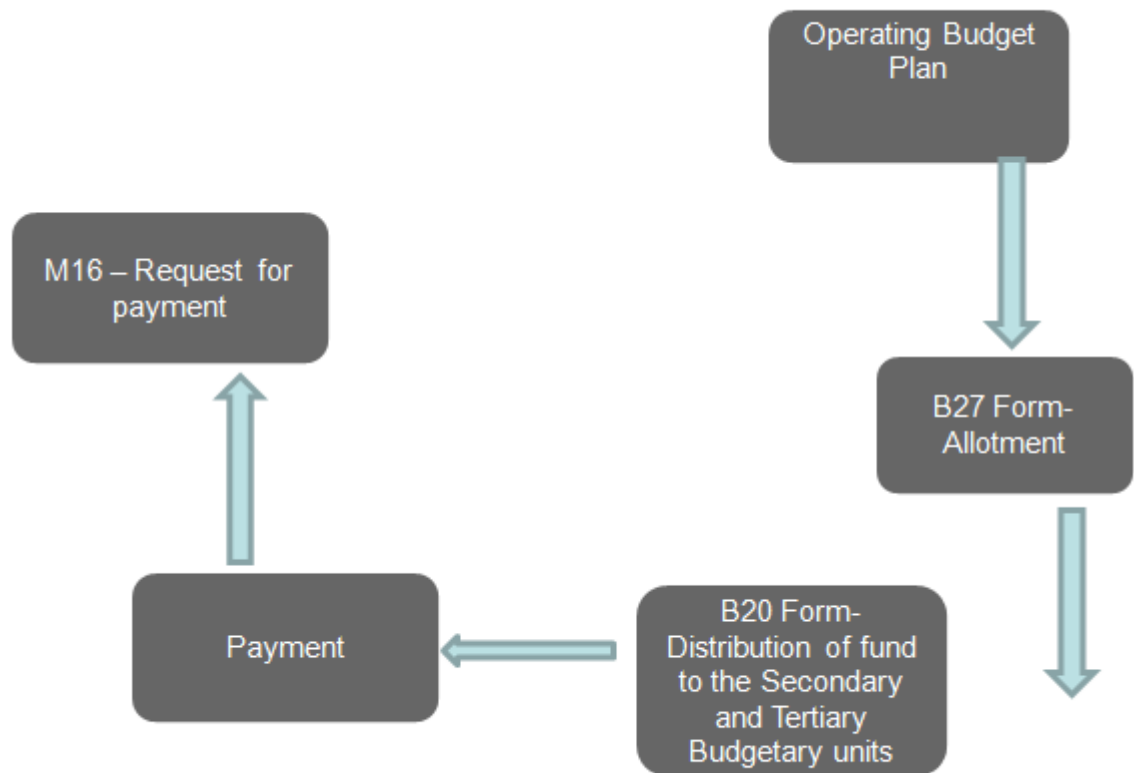


Figure 4: Operating Budget Allotment Cycle

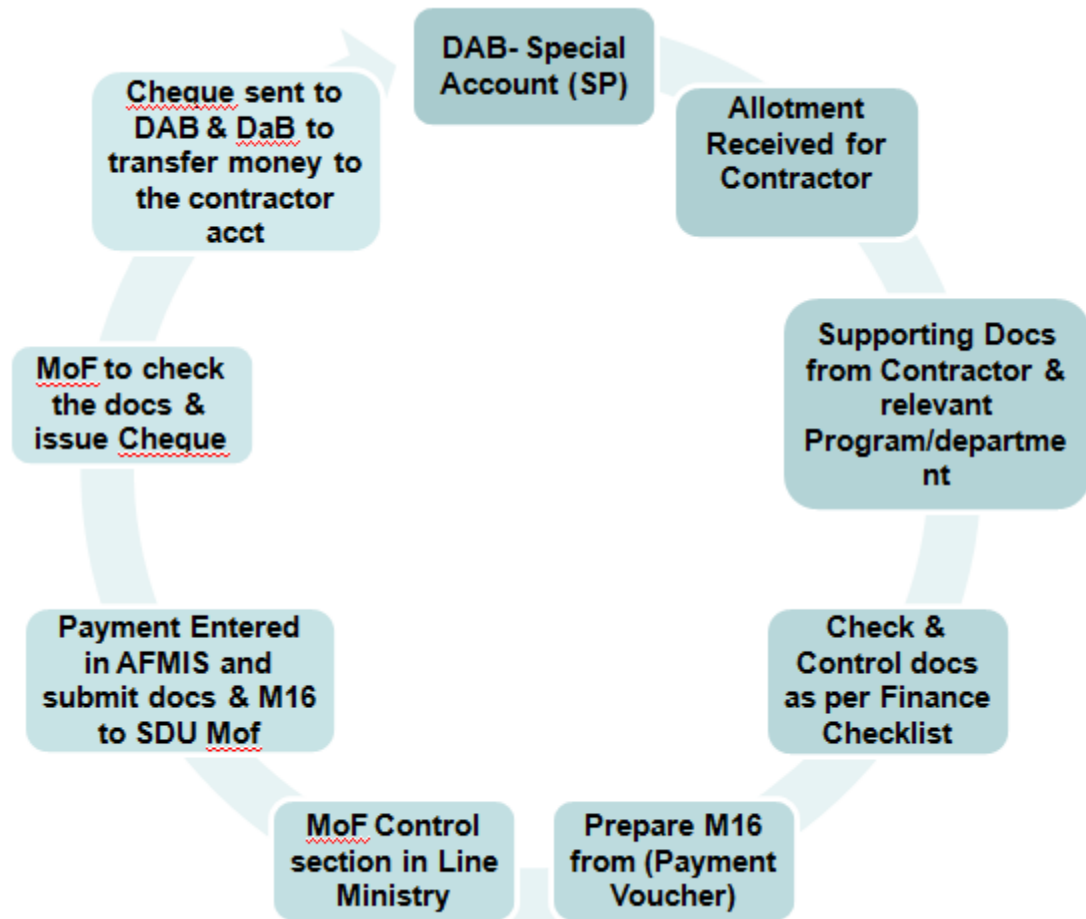


Figure 5: The Payment Process for Central Projects

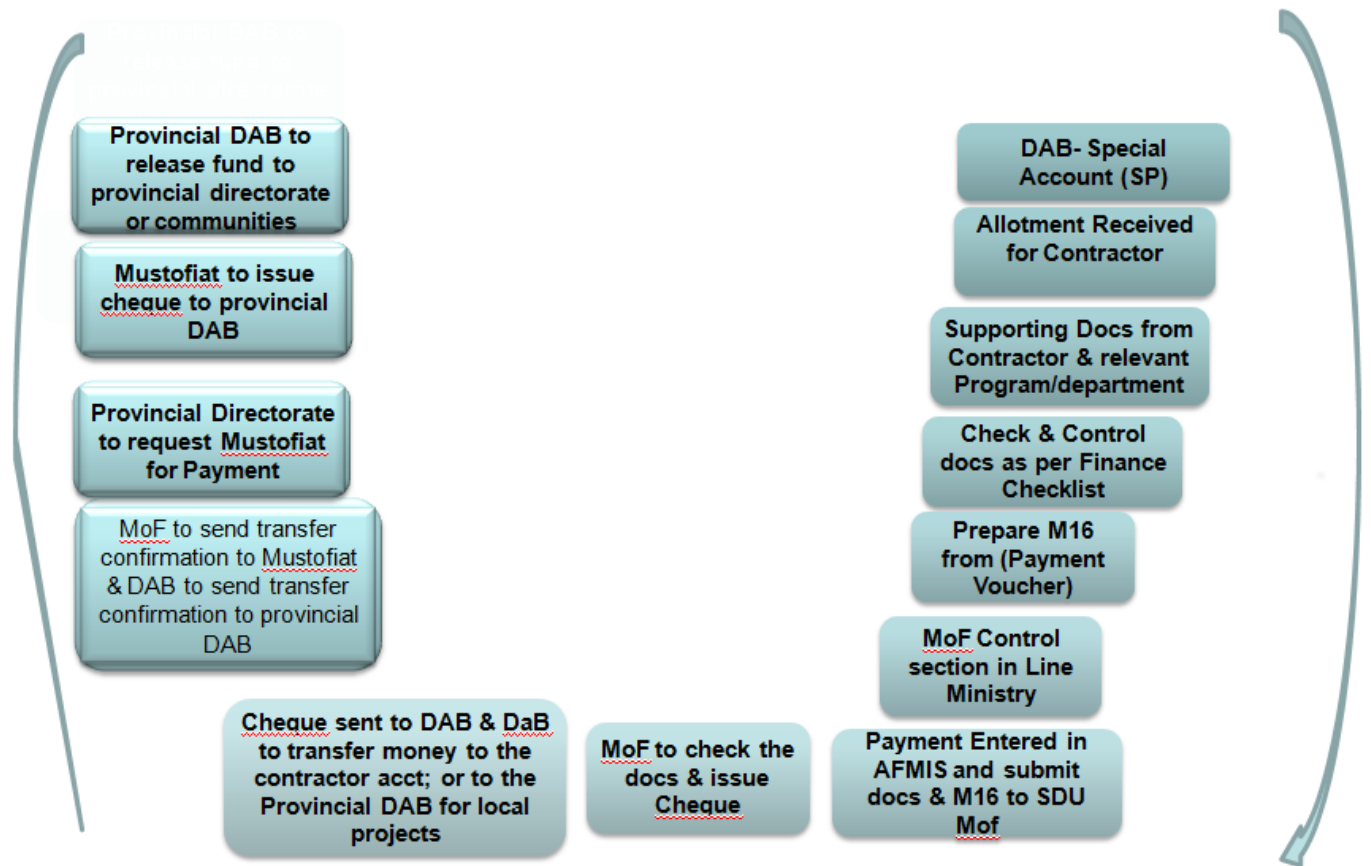


Figure 6: The Payment Process for Local Projects

APPENDIX B: LIST OF INTERVIEWS

No	Name	Title	Agency
MOF			
1	Ahmad Javed Jalali	DG Budget	MoF
2	Shafiqullah Amini	Infrastructure Sector Budget Specialist	MoF
3	Dr. Danny L. Athanasaw	US Treasury Advisor	MoF
4	Najimullah Qasimi	Provincial Budgeting Manager	MoF
5	Neak Mohammad Mohibi	Infrastructure Sector Manager	MoF
6	Musa Kamawi	Director of HR	MoF
7	Eng. Allawdin Zalmai	Performance Evaluation and Reporting Manager	MoF
8	Mr. Weshal Gandhi	Advisor to the Director General Treasury	MoF
9	Sayed Murtaz	Head of the Procurement Policy Unit - MoF	MoF
10	Mohammed Aqa	Director General Treasury - MoF	MoF
MAIL			
11	Mohammad Salim Kundozi	Admin& Finance Deputy Minister	MAIL
12	Mohammad Waheed Etabar	Director of Finance and Accounts	MAIL
13	Assadullah Noori	Director of Procurement	MAIL
14	Khalil Ur Rahman Ghznawi	Sector Manager	MAIL
15	Mr. Hotak		MAIL
MOE			
16	Faridullah Mirzad	Development Budget& AFMIS Manager	MoE
17	Samiullah Sherani	Internal Audit Officer	MoE
18	Mohammad Ismail Kettab	Director of Education Management Information System (EMIS) & System Analyst	MoE
19	Ahmad Najib Baizayee	Human Resource Management General Director	MoE
20	Ziahul Haq Safi	Finance Director	MoE
Mazar Province			
21	Zabihullah Akhtari	Sectoral Director	
22	Dr. Mohammad Afzal Hadid	Chairman of Provincial Council	

23	Mohammad Ishaq Sarwari	Mustofi	
24	Qais Mir Rahen	Director of Education	
25	Katib Shams	Director of Agriculture	
Herat Province			
26	Jaji Bashir Ahmad Ahmadi	General director of Agriculture programs	MAIL Herat province
27	Dr. Abdul Zahir Faiz Zadah	Director of Herat provincial council	Herat Province
28	Basir Ahmad Tahiry	Director, MoED Provincial Directorate	
29	Ab. Karim Zargar	Acting Sectoral Director, Governor's Office	
30	Mohammad Fahim Noor Zaie	General Accounting Manager- Mustofiat	Herat Province
31	Mohammad Massoud Popal	Sectoral Budget Manager	Herat province Governors office
OTHER			
32	Javid	AFMIS Advisor	
33	Khwaja	DG Admin and Finance - IDLG	IDLG
34	Nargis Nehan	Director of the Afghanistan Accountability and Transparency Organization (focus group discussion on national budgeting)	AATO